NORTH DAKOTA GRAIN DEALERS ASSOCIATION

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May 12, 2000
By overnight delivery

Surface Transportation Board
Office of the Secretary
Case Control Unit
Attention: STB Ex Parte No. 582 (Sub-No. 1)
1925 K Street N.W.
Washington, DC 20423-0001

Re: Ex Parte No. 582 (Sub-No. 1)

Enclosed is an original unbound statement in this proceeding on behalf of the four parties identified on the coversheet, plus 25 copies stapled. In addition, a 3.5-inch IBM-compatible floppy diskette is enclosed, on which an electronic copy of the statement has been placed in Microsoft Word 2000 format.

A copy of the statement is being sent to all Parties of Record today.

Sincerely,

NORTH DAKOTA GRAIN DEALERS ASSOCIATION

Steven D. Strege
Executive Vice President

Enclosures

Chc/STB/ltr 5-12

BEFORE THE

SURFACE TRANSPORTATION BOARD

RECEIVED
MAY 15 2000
RAIL MANAGEMENT
STB

Ex Parte No. 582(Sub-No. 1)
MAJOR RAIL CONSOLIDATION PROCEDURES

COMMENTS OF THE

NORTH DAKOTA PUBLIC SERVICE COMMISSION

NORTH DAKOTA GRAIN DEALERS ASSOCIATION

NORTH DAKOTA WHEAT COMMISSION

NORTH DAKOTA BARLEY COUNCIL

Due Date: May 16, 2000

BEFORE THE

SURFACE TRANSPORTATION BOARD

Ex Parte No. 582(Sub-No. 1)

COMMENTS OF THE

NORTH DAKOTA PUBLIC SERVICE COMMISSION
NORTH DAKOTA GRAIN DEALERS ASSOCIATION
NORTH DAKOTA WHEAT COMMISSION
NORTH DAKOTA BARLEY COUNCIL

North Dakota Parties & Introduction

This statement is submitted jointly by the North Dakota Public Service Commission, the North Dakota Grain Dealers Association, the North Dakota Wheat Commission, and the North Dakota Barley Council (North Dakota). These parties are identified in detail at the end of this statement.

North Dakota commends the Surface Transportation Board (Board or STB) for initiating this proceeding to look into if and how rail merger rules should be revised. As noted by the Board, the financial health and economic power of North American railroads are dramatically different than they were when the existing rules were promulgated shortly after passage of the Staggers Act. The industry is now healthy, as reflected by the fact that recent mergers have been accompanied by huge premium payments

The number of major carriers has also been reduced from over forty to only four in twenty years. This means that factors given heavy consideration in the merger application review process today should be different than those that were considered back in the early 1980's.

Breathing financial life back into struggling railroads by allowing them to rationalize their systems and the Nation's rail network is no longer a priority consideration – the job is largely done. North Dakota concurs that the focus of future merger application reviews must change. In the current environment and for the foreseeable future, shipper concerns should be given more consideration than in the past.

North Dakota has been directly impacted by past mergers, both by those involving carriers that serve the state and by those involving carriers that operate in other parts of the country and continent. We would like to focus our comments in the following areas:

- Downstream Effects - Anticipated Responses By Remaining Railroads
- Service Disruptions – Insuring Quality Service
- Impacts of Expanded Monopoly Power
- Promoting and Enhancing Competition
- Providing Continuation of Vital Short Line / Regional Rail Service
- Cross-border Issues
- Employee Protection

North Dakota's observations, concerns, and suggestions are presented in the paragraphs that follow.

Downstream Effects

The Board is absolutely correct and is to be commended for proposing that future merger applications be reviewed with an eye towards not only the direct impacts of the merger but also the long-term ramifications of the proposal. The field of "players" in the rail industry has been reduced to such a small number that the actions of one cannot help but affect all the others. When the number of Class I carriers declined, through merger, from 44 to 43, the "downstream" impacts were minor. When the number dropped from 6 to 5, the impacts were felt across the rail industry by both shippers and carriers. Every action naturally causes those impacted to respond as their own best interests dictate and as their abilities allow.

Service Disruptions – Insuring Quality Service

Merger proposals must include ironclad guarantees that service will not worsen. Likewise, merger proposals should clearly specify the measurement methods for determining service levels. Sufficient nonperformance penalties and enforcement mechanisms must be put in place. Detailed merger implementation plans should be required of applicants and be thoroughly reviewed by the Board. Deficiencies must be corrected before applications are approved. Applicants should pay for this review because they will be the beneficiaries of resulting merger efficiencies. The STB must provide oversight during the merger implementation, and include affected shippers in that process. The magnitude of future mergers makes it absolutely imperative that merger-precipitated service disruptions not occur again because the impacts can no longer be localized or regionalized. If they occur, they will have a crippling effect on major portions of the country. To protect the public and shipper interest, the Board must adopt rules and review procedures that will insure that these disruptions do not occur. These procedures should include surveying shippers who have been affected by past mergers. Many North Dakota shippers were impacted more negatively from recent mergers than what the carriers now portray.

Impacts of Expanded Monopoly Power

In its ANPR, the Board stated, "Other parties suggested that merger applicants be required to submit plans for preserving service options available to small shippers (e.g., grain shippers located on shortline railroads that cannot handle the newest generation of heavy railcars or load trains of a length/volume as may be required by practice of individual Class I carriers). This touches on an extremely significant problem.

As railroads become larger, their dependence for revenue generated from each individual shipper gets smaller. Increased monopoly power affects not only the railroads' ability to charge higher rates, it also enables them to demand that shippers customize their operations to suit the railroad's wants and needs rather than vice versa. This message has been delivered very strongly to grain shippers in the northern plains since

1980 and especially in the late 1990s, a time of major mergers. We feel this is more than just a coincidence.

These demands have had significant impacts on not only grain shippers but also on farmers, local communities, and local infrastructures. The railroads' demands for larger and larger consignments and shorter and shorter loading times have forced grain shippers to expand, either on their own or via consolidation. Depending on how much is spent, incentives may not be enough to pay for the investments made in facilities to meet the railroads' demands. Shippers have worked with railroads and invested heavily for greater efficiency. Every time the railroad increases required shipment sizes, more shippers are placed at a disadvantage and perhaps forced out of business. Not long ago in this region of the country a 52 or 54 car train loader was a "big" shipper in terms of loading capacity. Now, the major carrier in our region is pushing for trains double that size. The greater emphasis on higher volume crops and shipment sizes also means less emphasis on lower volume crops and shipment sizes. These specialty crops and niche markets may be the most profitable for growers.

Total grain production in a certain geographic area does not change when a railroad demands larger trains; this volume simply congregates at fewer points. So, as some shippers expand, others lose volume, and some are eventually forced out of business.

In the last dozen years the number of grain elevators in North Dakota has declined from nearly 600 to less than 450. The loss of local markets for farmers' grain has forced farmers to haul their grain farther to access the nearest grain elevator. As haul lengths have increase, naturally so have truck sizes. Now, instead of farmers hauling 300 bushels per trip to an elevator 10 miles away, they are hauling up to 1000 bushels per trip to elevators located up to 100 miles away. The impact on light density local roads and state highways has been immense. Increased market power has enabled the railroads to shift the cost of their infrastructure from themselves to the elevator industry, farmers local communities, and the public sector. What railroads see as efficient for themselves may not add efficiency to the entire movement chain from farmer to processor or exporter. No other participant in the chain has quite the economic power of the railroad to enforce such demands.

Before more railroads are allowed to merge, protections must be established to insure that ever-larger railroads cannot use their increasing economic power to restructure the grain industry to their vision, simply because they have the muscle to do so.

Service disruptions may be temporary but monopoly powers, both pricing and dictated service levels, are forever. Safeguards must be put in place.

Promoting and Enhancing Competition

The STB's stated goal in the ANPR is "promoting and enhancing competition" rather than just preserving what little is left. Future rules and procedures must promote and enhance competition. It is obvious that future mergers will significantly enhance the remaining carriers' market power to the detriment of the shipping community. The STB must be diligent in its quest to offset this newfound monopoly power with mechanisms that create shipper choices and force railroads to aggressively compete for shipper business rather than dictating prices and shipping requirements to them.

North Dakota supports some suggestions that have been made: A) Keep all existing rail gateways open, both physically and economically. B) Guarantee reciprocal switching at competitive rate levels. C) Avoid the creation of new bottlenecks by requiring the new merged railroad to quote rail users a separately challengeable rate to a competing carrier. We also support remedying existing bottlenecks as well, but that is not the subject of this proceeding.

Other specific proposals for promoting or enhancing competition will likely be proposed by other parties. The STB should simply commit itself to making the promotion and enhancement of competition a high priority item in any future merger case, and adopt all reasonable conditions for accomplishing those goals. Certainly there should be no diminishment in competition for any shipper. Where effective competition cannot be provided, shippers must be given reasonable, accessible and affordable means to obtain relief from abuse.

Providing Continuation of Vital Short Line / Regional Rail Service

Short line and regional railroads have become an asset to North Dakota. They have preserved and improved rail service in most cases. New merger rules must protect these service providers. Future merger proposals should include a clear self-imposed and STB-enforceable plan to maintain these important small carriers. Including the "Bill of Rights" proposed by the American Shortline and Regional Railroad Association in Ex Parte 582 in the proposed rules in this proceeding would bring about a full debate on their merits and demerits.

It appears that, in some cases, Class I carriers may believe that some of the short lines that they created shortly after the passage of the Staggers Act have now outlived their usefulness. Some short lines and regionals were created to forestall abandonments. They were aggressive service providers and they continued to generate traffic for the original owner.

Subsequent abandonments and mergers have made these operators less important to the original Class I owner. If these lines cease to exist, the lack of other transportation alternatives will simply cause this traffic to gravitate to the Class I's main lines. This occurrence will be further aggravated by the transition to larger cars and longer trains. Short lines and regional carriers have proven to be aggressive service providers that have helped bring economic development to depressed rural economies. The STB must not allow this advent to be stopped because of the market powers created by future mergers.

Cross-Border Issues

Farmers in northern plains states, including North Dakota, compete with farmers in the southern regions of the Canadian prairie provinces of Manitoba, Saskatchewan, and Alberta for spring wheat, durum wheat and barley markets worldwide. International trade agreements affect this relationship and influence cross-border flows of grain. This situation is made even more complex by the contrast of a free grain market system in the U.S. as compared to the domination and secrecy of the Canadian Wheat Board in Canada.

A railroad controlled in one country but operating in both can create additional distortions.

In our statement in Ex Parte 582, we pointed out a situation in northwestern North Dakota where it costs 18 cents per bushel more to ship grain by rail to Minneapolis than it does from a similarly situated station just a few miles away on the Canadian side of the border, even though both points are served by the same carrier. The Canadian Wheat Board has apparently pressured the railroad to give it a preferential rate advantage. No such leverage is available to shippers on the U.S. side of the border. U.S. farmers cannot take advantage of the lower Canadian rate because they are prevented from hauling grain into Canada. The rates charged U.S. shippers may not be challengeable before the STB but they are totally unreasonable and contrary to sound public policy.

If the STB is to approve further mergers that involve railroads operating across international borders, it must first put in place safeguards to protect U.S. farmers from manipulation and trade distortion. North Dakota has watched corn from southern Minnesota and Iowa move through our state to the Pacific Northwest at rates less than we pay for our own corn moving to the same market. We cannot afford to see Canadian spring wheat, durum wheat and barley take the place of our own grains in both domestic and foreign markets.

To address the potential for such abuses, the STB should adopt a rule which provides that:

> If a merger results in cross-border rail operations and shippers are confronted with rate differentials that put them in an uncompetitive situation, they will be guaranteed rates that are no higher than those offered at comparable shipping points located across the border.

The need to address this situation was highlighted again on May 10 when Transport Canada announced a mandated revenue cap on Canadian railroads that will reduce current year total grain freight revenues by an estimated 18% for the year beginning August 1, 2000. This will further distort cross-border rate comparisons. North of the border the government takes an aggressive role in controlling rail rates. South of the border the railroads have a much freer hand. Huge rate discrepancies result. U.S.

producers are not able to take their grain across the border to gain access to the lower rates. The end result is a major marketing disadvantage for the U.S. side of this production region.

Questions of regulatory authority arise when one railroad operates in two nations. How much authority does the STB have over a railroad operating in the United States but which is headquartered in Canada? An assumption that U.S. authority oversees operations in the U.S. while Canadian authority oversees operations in Canada, is not sufficient when actions on one side of the border affect that railroad's shippers on the other side. The rate situation mentioned above is one example. Another is car supply.

There are probably some advantages to a railroad operating on both sides of the U.S.-Canada border, in being able to shift its car supply for a commodity like grain, which has seasonality. That flexibility will no doubt lead to debate over which side is getting its "fair" share. Given the leverage of the Canadian Wheat Board as described above, there is a legitimate concern that such influence could affect car supply to the disadvantage of U.S. shippers.

The STB should deal with this matter in its new rules. North Dakota already deals with another carrier headquartered in Canada, but with operations in the U.S. That carrier strives to build shipper confidence in fairness by disclosing fleet numbers. It is, however, a much smaller operation, and does not cover larger regions of the United States like another merger across the border is likely to do.

Employee Protection

Labor protection is certainly a very sensitive subject. No one likes to see jobs lost and families disrupted. It is also important to note, however, that the cost of labor protection agreements is ultimately borne, at least in part, by shippers and the public.

We have pointed out that short lines and regional railroads have been good for North Dakota. We believe that the creation of these carriers would have been seriously curtailed had six years of labor benefits been prescribed. This prescription would have negatively impacted farmers, shippers, rural communities and, in fact, rail labor.

The lines that are operated by these new carriers are generating more traffic than they did when they were operated by Class I roads. Virtually all of this traffic is interlined with Class Is. These carriers are, therefore, generating jobs for union labor on Class I carriers.

Extreme care must be taken when consideration is given to establishing new or expanded labor protection rules. As stated earlier, the cost of these protections is ultimately borne, at least in part, by shippers and the public. Fairness is certainly an issue but the Board must recognize who will bear the costs.

Conclusion

By not commenting on some of the other topic areas in the ANPR – safe operations, "three-to-two" issues, and public interest benefits – we do not mean to slight them. Our concentration was on the issues most important to us.

In hindsight, this proceeding might better have been initiated in the early 1990's prior to the last round of transactions – UP-CNW, BN-SF, UP-SP, CN-IC, and NS-CSX-Conrail. But that is water under the bridge. The STB should continue to move forward boldly with this proceeding to see that shippers, receivers, and general public interest are protected in future transactions.

North Dakota Parties

North Dakota Grain Dealers Association - The North Dakota Grain Dealers Association (NDGDA) is an 89 year-old voluntary membership, nonpolitical trade association of grain elevators in North Dakota. More than 90% of the state's 450 grain elevators are members of NDGDA. Country grain elevators are the first point of sale for most crops grown by North Dakota farmers. These elevators clean and blend grain and ship it to both domestic processors and export ports. These destinations are generally located between 300 and 1500 miles from North Dakota and, given the state's lack of navigable waterways, are accessible only by rail. Trucking is a limited option due to distances to markets and the large volumes of bulk grain.

Approximately 90 percent of North Dakota's grain elevators have rail service; less than 3 percent have direct access to more than one carrier. Elevators with rail service handle about 95 percent of the grain marketed annually by local farmers. Approximately 70 percent of all the grain sold by grain elevators each year is moved to market by rail.

North Dakota is served by two Class I railroads. Burlington Northern Santa Fe and its short line affiliate, the Red River Valley and Western, serve about 75 percent of the elevators that have rail service. The other 25 percent are served by the Canadian Pacific Railway or it short line affiliates, the Dakota, Missouri Valley and Western or Northern Plains Railroad.

Transportation is vitally important to grain elevator operators. Without adequate and reasonably priced transportation services, elevators cannot sell and deliver their grain to distant buyers. These firms must cover their operating costs and earn a profit from a margin that equals as little as 2% of the cost of the commodity that they are handling. There is, quite simply, little room for error. Effective competition or meaningful regulatory oversight are essential to North Dakota's grain elevator industry and to the farmers that it serves.

Wheat Commission & Barley Council - The North Dakota Wheat Commission and the North Dakota Barley Council were created by the state legislature and exist to develop and service markets for wheat (flour), durum (pasta), and barley (malt for beer and grain for human and animal consumption) that is grown in the state. These Commissions are financed through voluntary per bushel payments that are made by North Dakota's 30,000 farmers when they sell the grain that they produce each year. Transportation is vital to farmers. If elevators cannot sell and deliver grain to distant markets, there ceases to be a local market for farmers' grain. North Dakota's physical location makes its impractical for these farmers to deliver their grain to distant terminal locations such as Minneapolis. They depend on local grain elevators to provide this crucial marketing link. If elevators are unable to provide a local market for farmers' grain, farmers are left with no viable alternatives.

Farmers indirectly pay to have grain sent from their local elevator to distant terminal markets. The costs that grain elevators incur when delivering grain to terminal markets directly impacts the prices that elevators are willing and able to pay farmers for their grain. High freight rates mean lower grain prices and lower farmer income. These factors also have a direct impact on the value of the land that farmers own since land values are directly related to the net income that farmers are able to realize from that asset.

Agriculture is North Dakota's number one business. Over fifty percent of the state's economy is dependent on agriculture. Without the ability to move its agricultural production to distant markets at reasonable and competitive rates, North Dakota's vast production capabilities lose all or part of their value. This proceeding is extremely important to North Dakota, its grain elevator industry, its economy, and individual farmers throughout the state.

North Dakota Public Service Commission - NDPSC is a three-member constitutional body that is charged with representing North Dakota's shipping interests in proceedings such as this. NDPSC has been active in Interstate Commerce Commission and Surface Transportation Board cases for well over one hundred years. This level of involvement is indicative of the state's need for reliable, reasonably priced transportation services and its lack of transportation alternatives.

CERTIFICATE OF SERVICE

Copies of the foregoing statement were mailed to Parties of Record in this by first class mail on this date.

Steven D. Strege, Executive Vice President
North Dakota Grain Dealers Association
Date: 5-12-00